No. 8425.

In the United States
Circuit Court of Appeals
For the Ninth Circuit.

9

ED HARDT,

Appellant,

vs.

JAMES MARTIN KIRKPATRICK,

Appellee.

PETITION FOR REHEARING.

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TOPICAL INDEX.

TABLE OF AUTHORITIES CITED.

STATUTES.

TEXT BOOKS AND ENCYCLOPEDIAS.

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To the Honorable the Above Entitled Circuit Court of Appeals:

The decision on appeal in this case has occasioned widespread discussion and comment among members of the bar, trustees, credit men and others engaged in, or concerned with bankruptcy practice. As a result of earlier decisions, fixed practices have developed in this district concerning secured creditors and their rights, and unsecured creditors and their protection in bankruptcy. These practices have redounded to the benefit of general creditors, and have promoted the more efficient administration of bankruptcy causes—without injury to secured creditors.

Because of the possible loss of such benefits, and because of the possible harmful effect upon orderly bankruptcy administration, and because of the existing conflict in the various circuit courts on the issues involved, the writer has prepared, and asks leave to have filed and considered, this brief on petition for rehearing.

The Legal Question.

1. "May the property of the bankruptcy estate be lawfully foreclosed and sold after adjudication without the consent of the bankruptcy court, in the absence of a prior restraint upon such foreclosure issued out of the bankruptcy court, where such property is in the possession of the bankruptcy court at the time of the commencement of the foreclosure proceedings?"

Or, stated as a corollary to the foregoing,

2. "Is the silence of the bankruptcy court, as evidenced by its failure to issue a prior injunction, tantamount to the consent by the bankruptcy court to a foreclosure and sale held after adjudication and without the approval of the bankruptcy court?"

The Practical Background of the Problem.

Before turning to a discussion of the abstract legal question involved, it is perhaps proper to discuss the objective realities which provide the background for and give rise to the instant problem.

In effect, by this decision, this court has said that where the bankruptcy court has not issued a prior stay, secured creditors are at liberty to proceed with foreclosure suits without notice to or consent of the bankruptcy court. The exact language of the decision is as follows:

> "Section 75 (s) of the Bankruptcy Act itself provides a direct and orderly means by which the court can prevent any such flaunting—the simple expedient of issuing a stay against the lienor's sale."

Let us examine, however, the factual situation and background in the ordinary bankruptcy case, in order to determine whether the remedy by prior stay is either simple or direct.

Manifestly, the provisions of the Bankruptcy Act are not self-executing. Human hands and brains must administer it and invoke its benefits and safeguards. Neither the District Court nor the Referee are so omniscient as to know, *sua sponte,* everything pertaining to the nature and extent of a bankrupt's holdings. Some person or officer of the court with knowledge of the facts, giving rise to the right to injunctive relief, must appear to obtain it; and if, for any period after the commencement of the bankruptcy proceedings, there be, as we shall attempt to show, no officer who could, nor person who in practice might, seek such relief, then of course, the court will be silent and no stay will issue.

Today when a voluntary petition in bankruptcy is filed, two to six weeks, on the average, elapse before the first meeting of creditors and the consequent election of the trustee. In involuntary proceedings, not less than five weeks, and oftentimes (dependent upon service, answer, trial, etc.) many months, pass before a trustee is elected. If a foreclosure sale can properly take place in the interim without the consent of the bankruptcy court, are creditors protected—should they suffer because of the absence of an intervening stay? No one could seriously argue that if, in the interim between the commencement of the proceedings and the election of a trustee, there were no person or officer who could or might be expected to seek a stay, all creditors should be bound by, and suffer as a result of, the natural silence of the bankruptcy court.

But it may be said that there are at least three classes of persons who could seek such a stay prior to the election of the trustee, viz.—

First—The Debtor—Bankrupt.

Second—The Receiver.

Third—General Creditors.

Manifestly, after his bankruptcy, a bankrupt is not overly concerned with his non-exempt property or the rights of the various classes of creditors with respect thereto. He has little, if any, stake in the ensuing conflict. Where there is no material or real interest, it is vain to expect the solicitude of a bankrupt for his creditors. To feel otherwise would be to turn our faces from the facts. If statistics were available they would show very few, if any, instances, notwithstanding the tens of thousands of bankruptcy cases, of proceedings initiated by bankrupts for the purpose of aiding one class of creditors as against another. Technically, the bankrupt might be heard (although he actually loses title by bankruptcy and thus has no standing in court); practically, he is never heard. Certainly the bankrupt's silence should not prejudice general creditors. No such relationship in law exists between the bankrupt and his creditors as to cause the latter to be bound *per se* by the silence or failure to act of the former.

Secondly, there is the receiver. The practice of appointing receivers in bankruptcy cases is frowned upon, save in instances of absolute necessity. (Bankr. Acts, Section 2, Sub. 3.) The added costs and expenses of receivers have been such as to cause the District Courts to adopt rules limiting and proscribing such appointments.

If we assume as a matter of law that a receiver could seek a stay, then the foregoing salutary rule against the appointment of receivers will be lost to creditors if, in order to be protected against the effect of extra-judicial foreclosures, such creditors must seek the appointment of a receiver who in turn might obtain the necessary stay. But when appointed, the receiver takes no title—his are the rights only of a custodian. To elaborate upon the instances in which a receiver may or may not act would prolong this discussion unduly. But the following cases indicate clearly the limitation upon the powers and rights of a receiver:

In re Maucuse, 11 Fed. (2d) 513—

> "It may not be amiss to make again a statement of the receiver's status and his duties. He is a statutory receiver appointed only when it is absolutely necessary.
>
> "He is not a partisan, with power to back one litigant against the other with the assets of the estate. Until the adjudication occurs, the contest is one between the creditor and the bankrupt. As between the two contending litigants, the receiver is neutral."

See also:

In re Benedict, 140 Fed. 55;
In re Magen, 3 Fed. (2d) 33;
Shubinsky v. Badek, 172 Fed. 332.

These cases reiterate the rule that the receiver is but a temporary custodian, entitled only to the possession of those things which are without dispute the bankrupt's. Being a temporary officer, he is generally not able to assemble properly all the information relative to the nature,

extent and lien upon the bankrupt's holdings. He should not be required precipitously to rush in seeking injunctive relief; he has scarcely the time, however, to do otherwise, even if we assume that he has the legal right to proceed,—a right which, until this Circuit Court rules squarely upon, is in grave doubt.

To sum up then, if the rule of this case becomes final and a stay must be sought, the grounds for the appointment of a receiver will be extended—notwithstanding the valid reasons against any such extensions; and such receiver, when appointed, may not have legal power to act, and generally will not have the practical opportunity of discovering the facts enabling him to act properly as an officer of the court.

Thirdly, it may be contended that the creditors themselves may seek the necessary stay. Whether they may do so is not clear. (See discussion in 1 Remington, Section 463, *et seq.*, p. 578 through 582.) But granted the legal right, what does and will happen practically? Creditors are located all over the country. Bankruptcy means often the end of creditors' connection with the bankrupt. Creditors' knowledge of the bankrupt's affairs is greatly limited to their dealings with him. The time, delay and expense of individual action by a creditor acts as a deterrent too powerful to be dispelled by the existence of a doubtful legal right. And such creditors have long felt and should, we submit, be entitled to continue to feel that the commencement of a bankruptcy proceeding is a *"caveat"* to the world—and that the *status quo* will be preserved by operation of law until the election of the trustee. It seems a harsh rule which would convert the sil-

ence of creditors, their failure to seek a stay in such cases, into a loss to creditors.

Thus far, we have dealt with the situation of a sale after bankruptcy, but before the election of a trustee. Like arguments for requiring notice to, and the consent of the bankruptcy court apply, as we shall hereafter show, with only slight diminished emphasis, to cases of foreclosure initiated after the election of the trustee.

What is the position of the secured creditor? Of necessity, his rights should likewise be protected—and are. By the positive provisions of the Bankruptcy Act (Section 67D), valid liens are not affected by bankruptcy. While the remedy of a secured creditor may be temporarily disturbed, substantive rights are not affected. Such secured creditor contracts with his debtor, presumptively with knowledge that the remedy of his contract is subjected to the possibility of the ensuing bankruptcy of his debtor. Such secured creditor knows where his security lies—knows where his debtor is located, receives notice of the bankruptcy. Now, as between the trustee, after his election and qualification, and such secured creditor, who is in the better position to proceed before the federal court in the first instance? The trustee, prior to his qualification, knows little, if anything, of the bankrupt's affairs. Oftentimes, the positions of the trustee and bankrupt are antagonistic. Much time must elapse before the trustee can assemble all of the necessary information. Such information is often withheld from the trustee—more often,

it is obtained only with difficulty. These statements may be generalizations, but they are unfortunately all too true.

Is it then too much, under such circumstances, to ask that the secured creditor be required to give notice to and seek the consent of the bankruptcy court, before proceeding with his foreclosure? Courts of bankruptcy are a part of the equity side of our Federal Judiciary system. It would be unfair to presume that if the consent of this court were sought, that it would be arbitrarily refused (and to do so would be reversible error).

Upon petition filed for leave to foreclose, notice is thus given to the estate in bankruptcy, and its officers can then intelligently proceed to determine the nature and extent of the liens upon the encumbered property, check into their validity, and determine the possibility of an equity for general creditors, etc.

We submit that on every conceivable practical ground, and especially for the sake of the better administration of bankruptcy causes, and because it is not a burdensome requirement to impose upon secured creditors, that the rule should be followed as laid down in the Eighth Circuit Court of Appeals in the case of *Comer v. John Hancock Mutual Life Insurance Company,* 80 Fed. (2d) 413—in cases where foreclosure is initiated after bankruptcy, and where the property is in the possession of the bankruptcy court, that the lien holder must procure the consent of the bankruptcy court as a condition to a lawful foreclosure of his security. We shall attempt to show that as a matter of law this rule is sustained by a very respectable weight of authority.

Discussion of the Law.

Admittedly, in the case at bar, no court other than the bankruptcy court had taken jurisdiction of this real property. No state court proceedings, or other proceedings, judicial or otherwise, had been instituted by the trustee under the trust deed at the time of the adjudication in bankruptcy. In its opinion, this Circuit Court states:

> "We are assuming for the purpose of this case that such proceedings were initiated after the adjudication of bankruptcy."

Therefore, those cases are unimportant which involve instances where a court of competent jurisdiction had, prior to bankruptcy, assumed control of the *res* in actions involving admittedly valid liens thereon. Likewise, those cases involving instances where proceedings to foreclose have been instituted before bankruptcy, are not determinative of this issue of the case at bar. A rule different from that which obtains in the two classes of cases mentioned above exists where the property is in the possession of the bankruptcy court prior to the time when the foreclosure is instituted.

Perhaps the most succinct statement of this distinction is made by Remington in his work in bankruptcy in Volume V, Fourth Edition, at page 126:

> "AND OF COURSE, WHERE THE FORECLOSURE IS NOT INSTITUTED UNTIL AFTER THE FILING OF THE PETITION, AND THE PROPERTY IN QUESTION IS NOT ADVERSELY HELD AT THE TIME OF SUCH FILING, THE PROPERTY COMES INTO THE POSSESSION OF THE BANKRUPTCY COURT, WHICH OBTAINS COMPLETE JURISDICTION, AND THE FORECLOSURE SUIT CAN ONLY BE CARRIED ON WITH THE CONSENT OF THE BANKRUPTCY COURT." (Capitalization ours.)

The following cases are cited by the text writer in support of his statement:

Isaacs v. Hobbs, 282 U. S. 734;

Hobbs Tie v. Isaacs, 61 Fed. (2d) 1006;

1st Trust Company v. Baylor, 1 Fed. (2d) 24;

Prudential Insurance Company v. Prebyl, 246 N. W. 351;

In re Gas Products Company, 57 Fed. (2d) 342.

Again the same text writer reiterates this rule in the following express language (Section 2554.50, 5 Remington, 4th Edition, pages 525-526):

"AFTER THE FILING OF THE BANKRUPTCY PETITION, FORECLOSURE PROCEEDINGS ARE NOT TO BE INSTITUTED AS TO PROPERTY IN THE POSSESSION OF THE BANKRUPT, OR OF HIS AGENT, OR OF AN OFFICER OF THE BANKRUPTCY COURT . . . UNLESS BY LEAVE OF THE BANKRUPTCY COURT IN THE EXERCISE OF ITS JUDICIAL DISCRETION. . . . " (Capitalization ours.)

Title and Trust Company v. Wernich, 68 Fed. (2d) 811 C. C. A. 9.

It will be seen that the foregoing statement of this text writer finds its authority in an opinion of this Ninth Circuit Court, that of *Title and Trust Company v. Wernich,* 68 Fed. (2d) 811. The opinion was written by Mr. Justice Wilbur of this court, and the rule summarized is as follows:

"At the outset, it should be stated that the matter of whether or not foreclosure shall be permitted rests entirely in the discretion of the bankruptcy court."

There is no more profound student of bankruptcy law than Mr. Remington; his recognition and pronouncement of the distinction contended for by the petitioner, especially when such pronouncement is supported by excellent authorities, appears very important and seems not to have been directed to this Honorable Court's attention in the former briefs.

This distinction is so important that it has likewise become the subject matter of a very lengthy annotation and collation of authorities found in 75 Lawyer's Edition, commencing at page 1060.

Manifestly, it is a far cry from the rule that foreclosure proceedings may not be instituted in the first instance unless by leave of the bankruptcy court in the exercise of its judicial discretion, to a rule which provides that a foreclosure may be instituted at any time, notwithstanding that the bankruptcy court has possession of the *res,* so long as this court does not take the initiative and issue a stay to restrain it.

This entire classification of authorities which turn upon the question of when the foreclosure is instituted with respect to the time of bankruptcy and possession of the *res,* would be a meaningless mass of authorities unless the principal contended for by the petitioner on rehearing became the devining rod and the determining factor in such cases; and we submit that it therefore cannot be said that there is no difference under the bankruptcy law between a case in which foreclosure is instituted before bankruptcy, and a case in which foreclosure is instituted after bankruptcy, and the *res* is in the possession of the bankruptcy court at the time of the institution of the foreclosure proceedings. In this latter event, it is, under

the authorities, a condition precedent to a valid foreclosure that the consent of the bankruptcy court be first obtained.

To state that the creditors in bankruptcy are not affected if the present decision of this Honorable Circuit Court in this case be made final because creditors, through their trustee, may file an independent suit to review the foreclosure proceedings, is in effect to state that there is fundamentally no difference between the absolute right to injunctive relief and the right of simple appeal. The entire philosophy of equity proceedings and relief by injunction is a negation of the argument implied by the present decision to the effect that creditors are uninjured because they can still review the foreclosure proceedings by appeal or review.

Since the cases indicate that the consent of the bankruptcy court is necessary, a question may arise as to what constitutes consent. Except in certain specified instances, of which the case at bar is not one, silence is not consent; and certainly there is nothing in the case at bar from which consent can be inferred, for the facts show that not only was this consent not given, but it was expressly refused.

There is a Supreme Court case which we submit is virtually on "all fours" with the case at bar. We refer to the case of *Dayton v. Stanard,* 241 U. S. 588. There the bankruptcy court was in possession of real property. After bankruptcy, the taxing authorities sought to have the property sold for taxes accrued prior to the bankruptcy. The authorities proceeded to a tax sale without the consent of the bankruptcy court. (Clearly no injunction had been sought by the trustee, for then the question would have been moot, as no sale would have taken place

—rather is this a case where the trustee was silent until after the sale.) In passing upon the question of the validity of such a sale after bankruptcy, in the absence of the consent of the bankruptcy court, and in the absence of the exercise by it of its injunctive powers, the Supreme Court clearly states:

> "This is a controversy growing out of the sale for taxes and special assessments of divers tracts of real property belonging to a bankrupt estate then in the course of administration in a court of bankruptcy. The property was in *custodia legis,* and was sold without leave of court. Because of this, the court held the sales invalid, and entered a decree cancelling the certificates of purchase and enjoining the County Treasurer from issuing tax deeds thereon. Thus far, there is no room to complain."
>
> *Wiswall v. Sampson,* 14 Howard 52;
>
> *Barton v. Barbour,* 104 U. S. 126;
>
> *Re Tyler,* 149 U. S. 164;
>
> *Re Eppstein,* 156 Fed. 42.

The latter case of *In re Eppstein,* 156 Fed. 42, at page 43, is a case in which Mr. Justice Sanborn participated. The opinion was written by Circuit Judge Van Devanter, who later became a Justice of the Supreme Court. Because of the fact that Mr. Justice Sanborn wrote the opinions in the case of *In re North Star Ice and Coal Company,* 252 Fed. 301, cited by this Circuit Court in its opinion, as well as the cited opinion in the case of *Southern Pharmaceutical Company,* 286 Fed. 148, we quote at length here from this *Eppstein* opinion:

> "Van Devanter, Circuit Judge. The Colorado Carlsbad Trade Company, a corporation existing

under the laws of Colorado, was adjudged a bankrupt upon the petition of creditors. Before the petition was filed, certain real property of the bankrupt had been sold for taxes, but the title, the right of possession, and the actual possession remained with the bankrupt, and these passed to the trustee upon his qualification. After the lapse of the three years designated in the redemption statute, and while the property was yet in the custody and control of the court of bankruptcy, as part of the bankrupt's estate, the holder of a tax sale certificate, without the leave of that court, applied to the County Treasurer and obtained a tax deed purported to invest him with all the right, title and interest of the bankrupt as the former owner. Thereafter, the trustee, learning of the sale and deed, tendered to the claimant thereunder the amount for which the property had been sold with statutory interest, penalties and costs, and demanded the surrender of title. The tender and request were refused and, upon the trustee's petition, the claimant was ordered to show cause why the deed should not be set aside. He appeared and objected that his right could not be adjudicated in a summary proceeding, whereupon the objection was sustained and the petition dismissed. The petition for reversion brings the matter here. The question of jurisdiction is not free from doubt, but we are of the opinion that the result of the cases is that a court of bankruptcy may by summary process require those who assert title to, or an interest in, property which has rightfully come into its possession and control as part of the bankrupt's estate, to present their claims to that court, and the notice being reasonable, may proceed to adjudicate the merits of such claims.

In re Kellogg, 121 Fed. 333;

In re Rochford, 124 Fed. 182.

> "The question of the merits must also, upon authority, be ruled in favor of the trustee. We do not mean that property in the course of administration under the bankruptcy act is exempt from taxation, or freed from tax liens or claims theretofore fastened upon it, BUT THAT IT IS IN CUSTODIA LEGIS, AND AND THAT ANY ACT INTERFERING WITH THE COURT'S POSSESSION, OR WITH ITS POWER OF CONTROL AND DISPOSAL, AND DONE WITHOUT ITS SANCTION, IS VOID." (Capitalization ours.)

Accordingly, Mr. Justice Van Devanter, with the concurrence of Mr. Justice Sanford, reversed the ruling of the trial court and flatly held such a sale, initiated after the commencement of the bankruptcy proceedings, and while the property was in the possession of the bankruptcy court, to be VOID in the absence of the consent of the bankruptcy court to such foreclosure.

To like effect is the case of *White v. Schloerb,* 178 U. S. 542. The rule that, when the property is in the custody of the bankruptcy court it cannot be sold or disposed of without its express consent, finds its support in the following additional United States Supreme Court cases:

Murphy v. John Hoffman, 211 U. S. 562;
Wabash v. Adelbert, 208 U. S. 38;
Harkin v. Brundage, 276 U. S. 457.

It would be vain to attempt to reconcile the rulings of, and the fair import of the decision in the case of *Isaacs v. Hobbs,* 75 Lawyer's Edition, 654, and *Comer v. John Hancock Mutual Life Insurance Co.,* 80 Fed. (2d) 413 (C. C. A. 8), with the decision in this case. The *Comer v. Hancock* case, *supra,* like the *In re Eppstein*

case, *supra,* both originate in the Eighth Circuit, and seem to follow the rule laid down there. But, we submit, these cases are much more consistent with the holding of the United States Supreme Court in the *Hobbs v. Isaacs* case, and in the *Dayton v. Stanard* case, *supra,* than is the present decision in this case.

There is yet another case in the Eighth Circuit to like effect, *First Trust Company v. Baylor,* C. C. A. 8, 1 Fed. (2d) 24:

> "Where the bankruptcy court has acquired jurisdiction of the *res,* the jurisdiction in bankruptcy will not be disturbed without its consent while the bankruptcy proceedings are pending. The trustee may, with the consent or under the direction of the bankruptcy court, abandon the property covered by the lien, and the bankruptcy court may grant permission to the mortgage creditors to foreclose in the state court."

Citing:

In re Zehner, 193 Fed. 787;

McHeney v. La Societe, 95 U. S. 58;

In re Bunn, 262 Fed. 527.

Again we reiterate that there can be no possible contention in the case at bar that permission to foreclose is inferable from the acts of either the Conciliation Commissioner or the District Court, for everything which was done by the District Court, or its officer, was a negation of such consent, either express or implied.

The case of *"In re Gas Products Company,* 57 Fed. (2d) 342," and that of *"McEldowney v. Card,* 193 Fed. 475 (C. C. A. 6)", involve discussions of what constitutes

consent by a federal court. In each of these cases, it required intervention by the bankruptcy trustee in the state court proceedings, and a prayer by the bankruptcy trustee, for affirmative relief, to spell out the necessary consent. Nowhere in either of these cases is the suggestion made that the mere silence of the bankruptcy court—its failure to issue a prior stay—creates the consent which is a condition to the further valid proceedings by the state court.

In reversing the District Court, this Circuit Court, in the present case, relies upon the following authorities, among others; and wherever such authorities are distinguishable from the case at bar, or fail to support *in toto* the rule of this case, we shall attempt to make such distinctions. This Honorable Circuit Court cites:

(a) *Hiscock v. Varick,* 206 U. S. 945. That case was decided in 1900, when the rule was that title did not vest in the trustee until the date of adjudication. The doctrine of relation back to the date of the commencement of bankruptcy had not then come into existence. Therefore, a sale after the institution of bankruptcy proceeding, but before adjudication, was held in effect to be a sale before the effective commencement of the bankruptcy proceedings themselves. The opinion in the case at bar clearly makes this distinction at pages 40 and 41 thereof, and we deem further discussion of the differences unnecessary.

(b) *North Star Ice and Coal Company,* 252 Fed. 301. That portion of the opinion which purportedly requires the issuance of a prior injunction is *obiter;* for the real question in that case, was whether a secured creditor

could participate at a meeting of general creditors, where such secured creditor had not alleged in his proof of debt the existence of a deficiency claim. In passing, it is interesting to note that the court in the *North Star Ice and Coal Company* case, cites the *Jersey Island Packing Company* case, (C. C. A. 9), 138 Fed. 625, although it is difficult to see what help is afforded by this latter case, for this *Jersey Island Packing* case, if carefully read, is authority for the position asserted by your petitioner.

(c) *Southern Pharmaceutical Company,* 286 Fed. 148. The issue before the court involved the attempted proof of an unliquidated claim in bankruptcy within sixty days after its final liquidation, but after the regular period for filing claims had expired. The point involved was the proper construction of Section 57N of the Bankruptcy Act; it was neither pertinent to nor necessary for that decision to enunciate any rule covering the issue in this case.

(d) *Dayton Coal and Iron Company,* 291 Fed. 390. At the time of bankruptcy there, the mortgaged property was in the actual possession of the Chancery Court of Rhea County, Tennessee, and that Chancery Court was properly administering that *res.* This, of course, is an example of the distinction in the cases, as made hereinbefore.

The foregoing cases cited by this Honorable Court do not then, we submit, sustain directly the rule laid down herein.

The case of *Robinson v. Kay* does support the present decision, excepting for the fact that the foreclosure itself was started before the bankruptcy proceedings commenced.

This case of *Robinson v. Kay,* and the case of *Heffron v. Western Loan and Building Association,* 84 Fed. (2d) 301, are alike in that they involve foreclosures instituted before the commencement of the bankruptcy proceedings. As this latter case is construed in the present decision, however, the factor of the time of the commencement of the foreclosure proceeding with respect to the time of bankruptcy, is made unimportant.

We submit that in this respect, the decision in the instant case is contra to the rule in the Eighth Circuit Court, and is likewise contra to the Supreme Court cases hereinbefore cited, and to the fair import of an earlier decision of this Ninth Circuit, to-wit, the case of *"In re Jersey Island Packing Company,* 138 Fed. 625."

We could in no event emphasize this distinction more clearly than by reiterating the argument made by Mr. Remington, and also by once more setting forth the express language of the Supreme Court in the *Isaacs v. Hobbs* case, *supra,* and the express language of the Eighth Circuit Court of Appeals in the *Comer v. John Hancock Mutual Life Insurance Company* case. Accordingly, we set forth the *verbatim* decision in the case of

> *"Isaacs v. Hobbs Tie and Timber Co.,* 282 U. S. 734"—
>
> "Mr. Justice Roberts delivered the opinion of the court:
>
> "In this cause the circuit court of appeals certified the following question:
>
> " 'After the bankruptcy court has acquired jurisdiction of the estate of the bankrupt and the referee therein has entered an order requiring sale, by the trustee, of all of the property of the bankrupt but

before the trustee has taken any steps to sell land (part of such estate) entirely located in another judicial district, can a suit to foreclose a valid mortgage thereon be commenced and an order of sale thereunder be made over the objection of the trustee, by the court of the latter district?'

"This court ordered that the entire record be sent up.

"The question correctly states the issue tried in the district court which entered the judgment from which the trustee appealed.

"Henrietta E. Cunningham was adjudged bankrupt in the northern district of Texas. The estate embraces land situate in the western district of Arkansas. B. K. Isaacs was elected trustee. Thereafter appellee, the holder of a note secured by a mortgage on the said land, instituted foreclosure proceedings in a state court of Arkansas. It named the bankrupt and Isaacs, the trustee, as defendants, recited the bankruptcy proceeding in the Texas district, and that it had not filed its secured note as a claim therein.

"The bankrupt and the trustee specially appeared and petitioned for removal of the cause to the United States district court for the western district of Arkansas. After removal the trustee filed an answer in which he set up, *inter alia,* his right and title as trustee, his lack of information as to the execution of the note and mortgage, and the fact that the land had been scheduled in the Texas district court as an asset of the bankrupt. He further averred that as trustee he had taken and then held peaceable possession of the land; that there was an equity in the same above the mortgage debt; that a sale in foreclosure would prejudice the rights of general cred-

itors; that he required time for investigation as to the most favorable method of sale; that neither he nor the bankruptcy court had consented to the foreclosure of the mortgage; that the bankruptcy court had entered an order authorizing him to sell the land; that that court had exclusive jurisdiction to ascertain the facts and administer the property; that the Federal district court in Arkansas could proceed no further than to ascertain the interests of the defendants, the validity of the mortgage lien, and the amount of the debt. The answer prayed that after these preliminary steps the court should refuse an order of sale, because of its want of jurisdiction to enter one.

"On motion of the plaintiff the court struck out so much of the answer as sought to delay judgment and sale, and entered, on the pleadings, a decree of foreclosure and sale containing a proviso that if there should be any surplus of purchase money, over the amount of the judgment, interest and costs, the same should be paid to the trustee.

"Upon adjudication, title to the bankrupt's property vests in the trustee with actual or constructive possession, and is placed in the custody of the bankruptcy court. Mueller v. Nugent, 184 U. S. 1, 14, 46 L. ed. 405, 411, 22 S. Ct. 269. The title and right to possession of all property owned and possessed by the bankrupt vests in the trustee as of the date of the filing of the petition in bankruptcy, no matter whether situated within or without the district in which the court sits. Robertson v. Howard, 229 U. S. 254, 259, 260, 57 L. ed. 1174, 1177, 33 S. Ct. 854; T. E. Wells & Co. v. Sharp, 125 C. C. A. 609, 208 Fed. 393; Galbraith v. Robson-Hilliard Grocery Co., 133 C. C. A. 46, 216 Fed. 842, 32 Am. Bankr. Rep. 752. It follows that the bankruptcy

court has exclusive jurisdiction to deal with the property of the bankrupt estate. It may order a sale of real estate lying outside the district. Robertson v. Howard, 229 U. S. 254, 259, 260, 57 L. ed. 1174, 1177, 33 S. Ct. 854, *supra; Re* Wilka (D. C.), 131 Fed. 1004. When this jurisdiction has attached the court's possession cannot be affected by actions brought in other courts. White v. Schloerb, 178 U. S. 542, 44 L. ed. 1183, 20 S. Ct. 1007; Murphy v. John Hofman Co., 211 U. S. 562, 53 L. ed. 327, 29 S. Ct. 154; Dayton v. Stanard, 241 U. S. 588, 60 L. ed. 1190, 36 S. Ct. 695. This is but an application of the well recognized rule that when a court of competent jurisdiction takes possession of property through its officers, this withdraws the property from the jurisdiction of all other courts which, though of concurrent jurisdiction, may not disturb that possession; and that the court originally acquiring jurisdiction is competent to hear and determine all questions respecting title, possession and control of the property. Murphy v. John Hofman Co., 211 U. S. 562, 53 L. ed. 327, 29 S. Ct. 154, *supra;* Wabash R. Co. v. Adelbert College, 208 U. S. 38, 52 L. ed. 379, 28 S. Ct. 182; Harkin v. Brundage, 276 U. S. 36, 72 L. ed. 457, 48 S. Ct. 268. Thus, while valid liens existing at the time of the commencement of a bankruptcy proceeding are preserved, it is solely within the power of a court of bankruptcy to ascertain their validity and amount and to decree the method of their liquidation. *Ex parte* City Bank, 3 How. 292, 11 L. ed. 451; Houston v. City Bank, 6 How, 486, 12 L. ed. 526; Ray v. Norseworthy, 23 Wall. 128, 23 L. ed. 116; *Re* Wilka (D. C.), 131 Fed. 1004, *supra;* Nisbet v. Federal Title & T. Co., 144 C. C. A. 54, 229 Fed. 644. The exercise of this function necessarily forbids interference with it by

foreclosure proceedings in other courts, which save fore the bankruptcy proceeding would be competent to that end. As mortgaged property ordinarily lies within the district in which the bankruptcy court sits, and the mortgagee can consequently be served with its process, the procedure usually followed is for that court to restrain the institution of foreclosure proceedings in any other. Where the land lies outside the limits of the district in which the bankruptcy court sits, ancillary proceedings may be instituted in the district court of the United States for the district in which the land is, and an injunction against foreclosure issued by the court of ancillary jurisdiction. *Re Patterson Lumber Co.* (D. C.), 228 Fed. 916 D. C.), 247 Fed. 578. Compare Security Mortg. Co. v. Powers, 278 U. S. 149, 73 L. ed. 236, 49 S. Ct. 84, 13 Am. Bankr. Rep. (N. S.) 86. Such injunctions are granted solely for the reason that the court in which foreclosure proceedings are instituted is without jurisdiction, after adjudication of bankruptcy, to deal with the land or liens upon it save by consent of the bankruptcy court. The appellant-trustee might have instituted ancillary proceedings in the district court for the western district of Arkansas and there obtained an injunction to restrain the appellee from foreclosing its mortgage. There is no reason, however, why he should not have followed the course here pursued, of pleading the adjudication in Texas in abatement of the foreclosure proceeding. The state court in which the foreclosure action was begun was without jurisdiction to pursue it. Upon removal into the federal court upon the ground of diversity of citizenship, the latter court had no higher or different right to interfere with the bankruptcy administration than had the state court. The answer of the trustee stated a

valid defence and it was error to enter judgment against him on the pleadings.

"Appellee asserts that inasmuch as the appellant removed the cause into the Federal court he waived any lack of jurisdiction in that court and estopped himself to set up exclusive jurisdiction of the bankruptcy court. There is no merit in this contention. The jurisdiction in bankruptcy is made exclusive in the interest of the due administration of the estate and the preservation of the rights of both secured and unsecured creditors. This fact places it beyond the power of the court's officers to oust it by surrender of property which has come into its possession. Whitney v. Wenman, 198 U. S. 539, 49 L. ed. 1157, 25 S. Ct. 778; *Re Schermerhorn,* 76 C. C. A. 215, 145 Fed. 341. Indeed, a court of bankruptcy itself is powerless to surrender its control of the administration of the estate. United States Fidelity & G. Co. v. Bray, 225 U. S. 205, 56 L. ed. 1055, 32 S. Ct. 620. The action of the trustee in removing the cause could not, therefore, divest the Texas district court of its jurisdiction.

"The judgment of the District Court must be reversed and the cause remanded to that court, for further proceedings in conformity with this opinion.

"Reversed."

Following the above case squarely is *Comer v. John Hancock Mutual Life Insurance Company, supra,* wherein the court states:

"We have no quarrel with the above case, but we are driven to doubt whether counsel for appellant,

in urging upon us abstract quotations from it, have not overlooked the concrete question up for judgment. This question was whether a mortgagee of lands situate in the State of Arkansas could wholly ignore the bankruptcy court and resort for a foreclosure of such lands to a court of Arkansas, when such lands were owned by a bankrupt in Texas whose estate was in course of administration, and a bankruptcy court held in the latter state. The Supreme Court held in the Hobbs case, *supra,* that neither the state court, nor even a federal court to which the action to foreclose was removed, had any power to oust the court of bankruptcy of its jurisdiction by merely ignoring the existence of the bankruptcy court, as was sought to be done in the Hobbs case, but it is a far cry from such a holding to that here contended for in the case at bar. Of course, a holder of a deed of trust containing a power of sale would have just as much right to ignore the bankruptcy court in foreclosure, as would a mortgagee who resorted to a strange court for strict foreclosure; THAT IS TO SAY, NO RIGHT AT ALL . . . for we think it clear that the principal announced by the Supreme Court carries an inhibition, both against foreclosure by a sale under the power in a deed of trust and a strict foreclosure in a court of equity, absent a lawful order by the bankruptcy court so permitting.

So, while the settled rule is that a bankruptcy court has the sole jurisdiction over the property of the bankrupt from which jurisdiction it may not be ousted without its consent, by any person or by any other court, regardless of liens thereon, it may as

> to an undisputed mortgage upon petition, and for cause shown for that there is no equity above the encumbrance, and for that the care of the property is therefore burdensome to the estate, order and permit that the lien thereon be foreclosed outside the bankruptcy court and in another state, or pursuant to a power of sale contained in a deed of trust."

The English language is powerless to convey any meaning if these cases do not expressly mean that the holder of the encumbrance must seek the consent of the bankruptcy court prior to foreclosing his lien, where at the time of the commencement of the foreclosure proceeding, the property is in the possession of the bankruptcy court. To read into these cases the implication that the foreclosure may lawfully be held unless the bankruptcy court first takes the initiative and issues a prior restraining order, is to give the decisions a meaning which they themselves do not contain, and which is not necessarily inferable from such decisions.

We submit, therefore, that the rule of the Eighth Circuit should be followed, and that the factual distinctions between the *Heffron v. Western Loan Building Company,* and *Kay v. Robinson* cases, *supra,* and the *Dayton v. Stanard* case, *supra,* should not be obliterated; if these factual distinctions are borne in mind, then the rule of the *Jersey Island Packing Company* case, decided by this court in 1905, may continue to prevail, and a uniformity of decisions established conformable to the various Su-

preme Court cases hereinabove cited. By so doing, this court will permit the continuance of a practice now being followed by most secured creditors who do seek the consent of the bankruptcy court before foreclosing.

The court will likewise, for the important practical reasons hereinbefore mentioned, give its continued assistance to the due administration of bankruptcy causes.

Respectfully submitted,

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By CHARLES J. KATZ,
Attorneys for Appellee.

I, Charles J. Katz, one of counsel submitting the foregoing petition for rehearing, [redacted] do hereby certify that said petition is, in my opinion, well founded, and that it is not interposed for delay.

CHARLES J. KATZ.